

REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE AND THE COUNCIL ON ELIAS MOTSOALEDI LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of Elias Motsoaledi Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and cash flows for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2012 (Act No. 5 of 2012) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

Basis for qualified opinion

Investment property

6. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for investment property. As described in note 5 to the financial statements, the restatement was made in order to rectify a prior year misstatement. I was unable to confirm the restatement by alternative means. Consequently I was unable to determine whether any adjustment to the investment property corresponding figure stated at R147 867 000 in the financial statements, was necessary.

Property, plant and equipment

7. I was unable to obtain sufficient appropriate audit evidence for an impairment amount of R10 276 900 included in the property, plant and equipment balance of R672 910 096 disclosed in note 6 to the financial statements. The municipality's records did not permit the application of alternative procedures. Consequently I was unable to determine whether any adjustment relating to the impairment of property, plant and equipment in the financial statements was necessary.
8. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding figure for property, plant and equipment. As described in note 6 to the financial statements, the restatement was made in order to rectify a prior year misstatement. I was unable to confirm the restatement by alternative means. Consequently I was unable to determine whether any adjustment to the property, plant and equipment corresponding figure stated at R183 051 381 in the financial statements was necessary.

Intangible assets

9. I was unable to obtain sufficient appropriate audit evidence regarding the intangible assets. I was unable to confirm the amount of the intangible assets by alternative means. Consequently I was unable to determine whether any adjustment relating to the intangible assets stated at R22 674 253 in the financial statements was necessary.

Irregular expenditure

10. Section 125(2)(d) of the MFMA requires the municipality to implement and maintain an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective. Payments amounting to R17 939 970 were made in contravention of the supply chain management requirements and was not disclosed note 51 to the financial statements.

Aggregation of immaterial uncorrected misstatements

11. The financial statements as a whole are materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following elements making up the statement of financial position and the statement of financial performance:
 - Revenue reflected as R72 289 042 is understated by R5 460 584
 - Consumer debtors reflected as R14 714 048 is understated by R5 421 160.
 - Payables from exchange transaction reflected as R28 375 003 is overstated by R4 502 584.

As a result, I was unable to determine whether any adjustments to these elements were necessary.

Contingent asset

12. The municipality has not disclosed a contingent asset in respect of the uncertainties arising from the dispute declared by the unions and the pending litigation regarding the wage curve agreement. I was unable to confirm the contingent assets by alternative means.

Value Added Tax (VAT)

13. The municipality entered into an agency agreement with its district municipality for the provision of water. As the agent, the municipality has accounted for VAT on the water transactions in contravention with the VAT Act. The municipality also entered into an agency agreement with the department of Roads and Transport for the collecting of license fees and issuing licenses and permits on behalf of the provincial government. The municipality did not account for output tax on the commission or agency fees for the services rendered in contravention with VAT act. Furthermore, the municipality claimed VAT on non-qualifying expenditure and also claimed the incorrect VAT amounts. I was unable to determine the

correct amount of the VAT receivable balance of R10 154 624 (2012: R7 878 000) as disclosed in note 45, as it was impractical to do so.

Opinion

14. In my opinion, except for the effects of the matters described in the Basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of Elias Motsoaledi Local Municipality as at 30 June 2013 and its financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA.

Emphasis of matters

15. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

16. As disclosed in note 45 to the financial statements, the corresponding figures for 30 June 2012 have been restated as a result of an error discovered during 2013 in the financial statements of the municipality at, and for the year ended, 30 June 2012.

Impairments

17. As disclosed in note 15 to the financial statements, the municipality made material impairments to the amount of R3 544 134 and R17 117 159 for receivables from exchange transactions and from non-exchange transactions respectively, as a result of inadequate collection practices.

Unauthorised expenditure

18. As disclosed in note 50 to the financial statements, the municipality incurred unauthorised expenditure of R38 681 636 as a result of exceeding the total amount appropriated for a vote in the approved budget.

Additional matters

19. I draw attention to the matter below. My opinion is not modified in respect of this matter:

Unaudited supplementary schedules

20. The municipality provided supplementary information in the financial statements on whether resources were obtained and used according to the legally adopted budget, in accordance with SA Standards of GRAP 1, *Presentation of financial statements*. The supplementary budget information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. Accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

21. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

22. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages XX to XX of the annual report.
23. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities or objectives. The usefulness of information further relates to whether

indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the *National Treasury Framework for managing programme performance information (FMPPI)*.

24. The reliability of the information in respect of the selected development priorities or objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
25. The material findings are as follows:

Usefulness of information

Presentation

Measures taken to improve performance not supported by sufficient appropriate evidence

26. Section 46 of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for 80% of measures taken to improve performance as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the validity of the measures taken to improve performance.

Consistency

27. The MSA, section 41(c) requires that the integrated development plan should form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 23% of the reported targets are not consistent with the targets as per the approved integrated development plan. This is due to the lack of developed internal policies and procedures for performance information management and reporting.
28. Section 25(2) of the MSA determines that an integrated development plan adopted by a municipal council may be amended in terms of section 34 and remains in force until an integrated development plan is adopted by the next elected council. Therefore, if the integrated development plan is changed in-year this process has to take place in accordance with the process as prescribed per section 34 of the MSA.
29. A total of 100% of targets reported in the annual performance report were changed in-year without following the process as prescribed in section 34 of the MSA and without adoption by the council of the municipality. This was due to a lack of monitoring and review mechanisms over performance reporting.

Measurability

30. The National Treasury *FMPPI* requires that performance targets be specific in clearly identifying the nature and required level of performance. A total of 25% of significantly important targets in relation to the core mandate of the municipality and being of significant public interest were not specific in clearly identifying the nature and the required level of performance. This was due to the fact that management was aware of the requirements of the *FMPPI* but chose not to apply the principles contained in the *FMPPI*.
31. The National Treasury *FMPPI* requires that performance targets be measurable. The required performance could not be measured for a total of 29% of the targets. This was due to the fact that management was aware of the requirements of the *FMPPI* but chose not to apply the principles contained in the *FMPPI*.
32. The National Treasury *FMPPI* requires that indicators/measures should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use. Hundred percent of the significantly important indicators in relation to the core mandate of the municipality and being of significant public interest were not well defined in

that clear, unambiguous data definitions were not available to allow for data to be collected consistently. This was due to the fact management was aware of the requirements of the *FMPP* but did not receive the necessary training to enable application of the principles.

33. The National Treasury *FMPP* requires that it must be possible to validate the processes and systems that produce the indicator. A total of 29% of the significantly important indicators in relation to the core mandate of the municipality were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the fact that management was aware of the requirements of the *FMPP* but chose not to apply the principles contained in the *FMPP*.

Reliability of information

Supporting documentation provided is not valid and accurate

34. The National Treasury *FMPP* requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the validity and accuracy of information presented with respect to the material development priorities for *Spatial Rationale and Infrastructure and Basic Service Delivery*. This was due the fact that the municipality could not provide sufficient appropriate evidence in support of the information presented with respect to these objectives

Compliance with laws and regulations

35. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Annual financial statements, performance and annual report

36. The annual performance report for the year under review does not include a comparison with the previous financial year and measures taken to improve performance, as required by section 46 (1)(a) of the MSA.
37. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of current assets, liabilities, expenditure, disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
38. The municipality did not establish a proper performance management system, as required by section 38(a) of the MSA.
39. The municipality did not have a proper internal control system for revenue and receivables as required by section 64(2)(f) of the MFMA.
40. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

Expenditure management

41. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.
42. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

HR Management

43. An acting CFO was appointed for a period of more than six months, in contravention of section 56(1)(c) of the MSA.
44. The CFO was appointed without having met the prescribed minimum competency levels as required by section 56(1)(b) of the MSA.

Internal audit

45. The internal audit unit did not report to the audit committee on matters relating to compliance with the MFMA, the DoRA and other applicable legislation, as required by section 165(2)(b) of the MFMA.

Strategic planning and performance management

46. The IDP adopted by the municipality does not reflect and identify the municipal council's vision for the long term development of the municipality and a financial plan, as required by sections 26 and 41 of the MSA.
47. The municipality did not give effect to its integrated development plan and conduct its affairs in a manner which was consistent with its integrated development plan, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
48. The municipality did not establish a proper performance management system, as required by section 38(a) of the MSA.
49. The performance management system of the municipality did not clarify the roles and responsibilities of each role-player in the functioning of the system, did not determine the frequency of reporting and the lines of accountability for performance and did not provide for procedures by which the system is linked to the municipality's integrated development planning processes, as required by section 38(a) of the MSA and Municipal planning and performance management regulation 7(2)(c).
50. The performance management system of the municipality did not provide for the monitoring of performance and for the measuring and review of performance at least once per year, with regard to each of those development priorities and objectives and against the key performance indicators and targets set, as required by section 41 of the MSA.
51. The performance management system of the municipality did not provide for taking steps to improve performance with regard to those development priorities and objectives where performance targets are not met, as required by section 41(1)(d) of the MSA.
52. The municipality did not set measurable performance targets for the financial year with regard to each of the development priorities and objectives and key performance indicators set out in the IDP, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulation 12(1) and 12(2)(e).
53. The accounting officer of the municipality did not by 25 January assess the performance of the municipality during the first half of the financial year, as required by section 72(1)(a)(ii) of the MFMA .
54. The internal audit did not adequately audit the results of performance measurements, as required by section 45(1)(a) of the MSA and Municipal planning and performance management regulation 14(1)(a).
55. The annual performance report for the year under review does not include a comparison with the previous financial year and measures taken to improve performance, as required by section 46(1)(b) and (c) of the MSA.

Internal control

56. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below

under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

57. Management does not always appropriately provide the required supervision and review over operations to ensure that the municipality complies with all laws and regulations and appoint the necessary skilled staff members.
58. Action plans regarding assets were not closely monitored, hence the recurring findings identified from the prior year.

Financial and performance management

59. The municipality did not formulate and implement a record management policy and related procedures to ensure that all documentation is properly controlled.
60. Management did not implement the following daily and monthly controls as designed for the entity's business processes:
 - Payments to creditors were not properly authorised by agreeing the payment to the detailed creditor statements.
 - The municipality did not perform reconciliations between the general ledger and the fixed asset register.
 - Adequate controls over daily and monthly processing and reconciling of transactions were not implemented.
61. Design and implementation of formal controls over IT systems to ensure the reliability of the systems and the availability, accuracy and protection of information was not implemented.
62. Regular, accurate and complete financial and performance reports that are supported and evidenced by reliable information was not implemented.

Governance

63. The internal audit function was outsourced for the year under review. The internal audit function did not have an approved internal audit charter for the year under review.
64. The municipality established an audit committee during the year under review. However it was found that the effectiveness of the audit committee was not assessed during the year under review.

Auditor-General

Polokwane

30 November 2013



Auditing to build public confidence